(19)

IN THE

Supreme Court of the United States

OCTOBER TERM, 1943.

No. 443

HARDEN MORTGAGE LOAN COMPANY, *Petitioner*,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT.

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The petitioner, Harden Mortgage Loan Company, a corporation, prays that a writ of certiorari be issued to review the judgment of the United States Circuit Court of Appeals for the Tenth Circuit entered in the above entitled cause on July 20, 1943.

OPINIONS BELOW.

The memorandum opinion of the United States Board of Tax Appeals (R. 11-20) is not reported. The opinion of the Circuit Court of Appeals (R. 50-54) is reported in 137 F. 2d 282.

JURISDICTION.

The judgment of the Circuit Court of Appeals was entered on July 20, 1943 (R. 54-55). The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED.

1. Whether petitioner, engaged in the mining and selling of rock asphalt (used for road building), is entitled to deduct as ordinary and necessary business expenses under Section 23 (a) of the Revenue Act of 1938 the sum of $32,937.75 paid in 1938 to one C. S. Beekman, or C. S. Beekman and Company, as commissions upon the sale of rock asphalt, when Beekman was an independent contractor, when the bulk of such sales was made to the Oklahoma State Highway Commission, and even though it be found and held that Beekman, or Beekman and Co., resorted to acts considered contrary to public policy in effecting such sales.

2. In the alternative, whether petitioner is entitled to deduct $16,893.70 of the aforesaid commissions, which amount was paid to C. S. Beekman, or his nominee, in January, 1938, on sales made by him in 1937 before any partnership was organized and when there were no alleged practices contrary to public policy.

STATUTE INVOLVED.

The statute involved is Section 23 (a) of the Revenue Act of 1938, c. 289, 52 Stat. 447, the pertinent part of which is as follows:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

(a) EXPENSES.—

(1) IN GENERAL.—All the ordinary and necessary expenses paid or incurred during the taxable year in

carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; traveling expenses (including the entire amount expended for meals and lodging) while away from home in the pursuit of a trade or business; and rentals or other payments required to to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity.

* * * * * * * * *

STATEMENT OF THE CASE.

Petitioner is a corporation engaged in mining and selling rock asphalt with its principal office in Oklahoma City, Oklahoma (R. 12). In 1938 it kept its books on the accrual basis (R. 25).

Rock Asphalt is a blend of limestone rock and asphalt and of sand and asphalt and is used as a road building material. It is sold principally to cities, counties, and states. (R. 12.)

In 1933 or 1934 petitioner entered into an agreement with C. S. Beekman Co., at face value certain claims which it tioner's rock asphalt on a ten per cent commission basis, which arrangement has continued to the present time. The agreement provided that Beekman was to receive his commissions only when petitioner received payment for the materials sold. C. S. Beekman had been acting as sales agent for producers of paving materials and pavements in the State of Oklahoma, and for contractors building state highways, for nearly 30 years. Not only did he represent producers other than the petitioner, but he also represents concerns selling road machinery and equipment. (R. 13.)

During 1937 Beekman made sales of rock asphalt to the Oklahoma State Highway Commission amounting to more than $170,000.00. By the end of that year the road building funds of Oklahoma had become exhausted and payments to petitioner were long delayed. In January, 1938, Beekman was short of funds and asked petitioner for an advance on commissions which would be due him when petitioner was

paid for the materials sold. Petitioner did not have funds with which to pay Beekman but assigned to his nominee, C. S. Beekman Co., at face value certain claims which it had against the State aggregating $16,893.70, which amount approximated the commissions which would be payable to Beekman on the material sold. (R. 13, 14, 29.)

In the early part of 1938 Beekman became almost totally blind and needed assistance in carrying on his sales work. He first called in his brother to assist him and, shortly after the State Legislature adjourned in the early part of 1938, he formed a partnership under the name and style of C. S. Beekman & Company, composed of himself, his brother, two members of the Oklahoma Legislature and another party who was more or less active in State politics. (R. 14.) The main task of Beekman and his partners was to carry on educational programs among the people in various sections of the State where roads were to be built in order to get them to demand rock asphalt roads (R. 17, 36, 46-47). After the partnership was formed Beekman asked petitioner, in drawing checks for commissions due him for rock asphalt sales, to make such checks payable to the order of C. S. Beekman & Co. This was done. (R. 14.)

In addition to the above mentioned assigned claims petitioner in 1938 paid to C. S. Beekman & Co. the sum of $16,044.05 as commissions on other sales. The total commissions paid by petitioner in 1938 amounted to $32,937.75. (R. 14.)

Petitioner sold its rock asphalt in Oklahoma at a uniform price of $4.25 per ton f.o.b. the mine (R. 13), and it kept the price posted in the Highway Department of the State at all times (R. 35). Petitioner exercised no control over Beekman as to how he spent his commission money and never instructed him with regard to whom he should approach in the matter of making sales (R. 34, 36, 47). Petitioner's vice-president and general manager did not know until long after 1938 that Beekman had formed his partnership, or who made up its membership, and he never met with the partners in a partnership meeting (R. 43-44, 48). Beekman never approached a State official or offered him money

to recommend petitioner's product and never paid any money for that purpose (R. 48).

In auditing petitioner's 1938 income tax return respondent disallowed as a deduction the selling commissions of $32,937.75 paid to Beekman & Company on the ground that payment thereof was against public policy (R. 8). The Tax Court and the Circuit Court of Appeals sustained respondent's action (R. 19, 54).

SPECIFICATION OF ERRORS TO BE URGED.

The Circuit Court erred as follows:

1. The Circuit Court erred (as did the Tax Court) in disregarding the uncontradicted testimony of C. S. Beekman, a witness on behalf of the respondent, and in assuming (contrary to such testimony—R. 47) that petitioner had knowledge of any alleged political influence on the part of Beekman and/or his associates in selling rock asphalt.

2. The Circuit Court erred (as did the Tax Court) in holding petitioner guilty of practices contrary to public policy, when petitioner merely contracted with Beekman, an independent contractor, to sell its product on a commission basis, even though it be held that Beekman and his associates did (unknown to petitioner) resort to practices contrary to public policy.

3. The Circuit Court erred (as did the Tax Court) in holding that petitioner is not entitled to deduct commissions paid to C. S. Beekman, or his nominee—Beekman & Co., even though it be held that Beekman and/or his associates resorted to political influence in order to make sales, and even though such fact was known to petitioner.

4. The Circuit Court erred (as did the Tax Court) in holding that petitioner is not entitled to deduct the commissions paid Beekman and/or his associates, on the assumption that they were guilty of practices contrary to public policy, when there are no facts in the record to support

such a holding, other than the fact that they had to deal with the agency set up by the State to receive them and deal with them, and in the manner prescribed by said agency.

5. In any event, the Circuit Court erred (as did the Tax Court) in holding that petitioner is not entitled to deduct that portion of the commissions paid by petitioner in 1938 on sales made by Beekman in 1937 at a time when Beekman had no partners and no associates, and when there were allegedly no practices on his part contrary to public policy.

6. The Circuit Court erred (as did the Tax Court) in holding that petitioner was not entitled to deduct the commissions paid to Beekman and/or Beekman & Co. in 1938 as ordinary and necessary business expenses under the provisions of Section 23 (a) of the Revenue Act of 1938, even though it be found that Beekman and his associates were friendly to the Oklahoma State Highway Commission, when there is no prohibition against such deduction in either the law or the regulations.

7. The Circuit Court erred in affirming the decision of the Tax Court.

REASONS FOR GRANTING THE WRIT.

The decision of the Tenth Circuit in this case is in conflict with decisions of the United States Circuit Courts of Appeals for the Fifth and Seventh Circuits in *Alexandria Gravel Company* v. *Commissioner,* 95 F. 2d 615, and *Heininger* v. *Commissioner,* 133 F. 2d 567, respectively. This Court granted a writ of certiorari in the latter of these cases, 319 U. S. ...., which case is now pending in this Court.

The Circuit Court of Appeals in the *Heininger* case held that the taxing statutes made no distinction between net income from a legal and an illegal business and that, for the Court to do so, would amount to judicial legislation. The Court said in that case—

> If the position of the respondent is sustained, and the attorneys' fees and expenses disallowed as a deduction in the instant case, then no business expense of an illegal business is deductible, and such business would be taxable on its gross income. *Congress has not said that that discrimination shall be made.* (Italics supplied.)

Petitioner does not admit that the record herein shows any conduct on its part or on the part of Beekman, the independent contractor who sold its product, which is contrary to public policy. If, however, it should be held that the commissions paid to Beekman & Co. were paid to that company for exerting political influence (and are, therefore, contrary to public policy), it is submitted that such payments still are deductible in computing taxable income because Congress has made no distinction between the taxable income of legal and illegal businesses.

The general principle is important and the phase of it involved in this proceeding should be considered by the Court along with the question in the *Heininger* case.

In any event, practices allegedly contrary to public policy in 1938, should not preclude deduction of $16,893.70, the commissions earned by Beekman in 1937—the year prior to the alleged illegal practices complained of herein.

Since the Court already has under consideration the identical question here involved, petitioner's rights should be protected until the issue is finally determined.

CONCLUSION.

It is therefore respectfully submitted that this petition for a writ of certiorari should be granted.

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